

Chapter 8

Risks related to key persons of service companies noted on the NewConnect*

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Introduction

The increase in the complexity of the circumstances in which companies currently come to do business generates a growing demand for risk management. In this chapter the author deals with one of the problems related to this domain of management, namely, the problem of the risk associated with key persons. The basic premise for this choice of research interest that was noticed by the author, both in the scientific literature and business practice, was the trend of a growing importance of key people in the contemporary management concepts and models. Being guided by the principle of logical consequence, the author came to the conclusion that risk associated with key persons is crucial regarding the probability of achieving success by companies. This intuition, however, required scientific confirmation, which gave rise to conducting both literature and empirical research devoted to the subject. The objectives of this study are of a cognitive nature and concern the identification of risk of key persons in the perspective of management processes and identification of ways of perception and the anticipated consequences and significance of this risk in the surveyed service companies.

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8.1. Risk management and risk related to key persons

The concept of risk management is most often combined with uncertainty. When it comes to uncertainty, one can assume that it refers to the lack of complete information about the future. In other words, uncertainty in management refers to the situation of decision-makers who have limited resources of knowledge necessary to describe the future results of the implemented actions (Elahi, 2013). Emblemvag and Kjolstad (2002) identify two basic types of uncertainty: fuzziness and ambiguity. The latter consists of discord and nonspecificity. The theoretical basis for explaining uncertainty consists of the probability theory and possibility theory. In terms of adverse events, risk may in turn mean uncertainty concerning the occurrence of a loss (Regda, 2007). In contrast, risk management, adopted in the narrower context, creates an expectation of decidability and management of uncertainty (Power, 2007). Risk management is a process that identifies loss exposure faced by an organization and selects the most appropriate technique for treating such exposures.

Elahi (2013) refers to risk management as an issue of growing interest and popularity. What proves the above statement, according to this author, is:

- increasing importance of risk management to the rank of strategic actions,
- presence of risk management as an essential component of virtually all current major management concepts (including supply chain management),
- transition of risk management from the phase of abstraction, through the rationalization phase, to the expansion phase (starting in the mid-90s of the last century),
- regarding risk-taking by organizations as a source of competitive advantage.

Risk management, as a relatively autonomous management domain, consists of many activities. These include, among others (Elahi, 2013):

- cultivating a risk awareness culture,
- setting proper levels of risk appetite in different parts of the organization,
- recognizing potential risks,
- detecting an evolving or happening risk,
- assessing the likelihood and impact of risks,
- assessing the potential benefits and opportunities associated with risks,
- categorizing and prioritizing risks,
- transferring/sharing risks,
- preventing/reducing the probabilities of risks,
- mitigating the impact of risks,
- reducing the sensitivity of the organization to risks through flexibility and agility,
- the ability to quickly recover from a realized risks.

The risk-based approach is now very popular in strategic management. This approach improves the organization's capability to capture the profitable opportunities envisioned by its strategies (Sheehan, 2010). The use of strategy maps to identify risk recognizes cognitive perspectives, such as: customer perspective, process perspective, learning and growth perspective.

In deliberations on what is also important there also appears its hierarchy. The hierarchical point of view led to the establishment of the so-called strategic risk. The concept of strategic risk is defined in close liaison with the concept of strategy. According to Emblemavag and Kjolstad (2002), strategic risk can be regarded as risk that arises in pursuit of a business objective. Such an understanding of strategic risk appears to prejudice that strategic risk is not probabilistic (in the calculus sense) because they are not necessarily all exhaustible nor mutually exclusive. The most famous and popular approach to strategic risk analysis is the SWOT analysis. The risk analysis includes in this case four basic steps (Emblemavag & Kjolstad, 2002): define objectives, brainstorm risks and characteristics according to the SWOT axis, calculate possibilities and consequences of the risks, combine risks with characteristics.

The consequence of separating strategic risk is the creation of the domain of strategic risk management. The components of the scope of strategic risk management include (Calandro, 2015):

- exposure concentrations,
- periphery monitoring,
- ambiguous threat analysis,
- risk mitigation,
- risk tracking,
- managing the integrity of the business model.

Kendrick (2004) indicates two key dimensions to the strategic understanding of risk within an organization. The first is the issue of understanding organizational and personal attitudes to risk, which will provide an attitude and behaviour dimension. The second one is an external and internal environment dimension.

Earlier considerations point to the importance of identifying the risk management process. Tchankova (2002) believes that the primary task of risk identification is to answer three basic questions:

- How can organizational resources be threatened?
- What adverse effect can prevent the organization from achieving its goals?
- What favourable possibility can be reviewed?

The main components of risk identification can be: source of risks, hazard factors, perils, exposures to risk.

The conducted literature analysis gives rise to conceptualize the role of risk of key people in management processes, as shown in Figure 8.1.

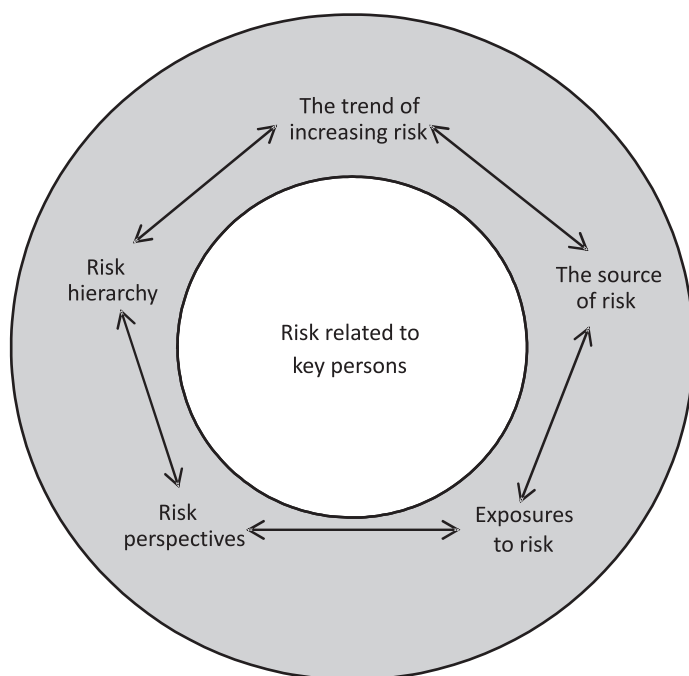


Figure 8.1. *The importance of key persons in risk management processes.*

The risk referred to has the following meanings:

- it can significantly contribute to the strengthening of trends associated with a significant increase of importance of risk in the organization's activities, including through the so-called interconnected risk,
- it is present in all key cognitive perspectives used to identify risks,
- it may be of strategic importance to the organization,
- it can co-create the dimension of understanding risks associated with the internal environment,
- key personnel is one of the resources exposed to risk.

8.2. Research methodology

This empirical research constitutes the continuation of research devoted to the analysis of the risk associated with business activity of service companies listed on the NewConnect.

The NewConnect is an alternative trading system that was created by the Warsaw Stock Exchange and has been operating since 2007. According to its

founders, the NewConnect is intended for small and rapidly growing companies that have a clear development strategy for whose funding they need capital amounting to tens of millions of zlotys (Przewodnik, 2015). For potential investors, the purchase of shares of companies listed on NewConnect is associated with a certain level of investment risk. The intention of the creators of NewConnect is to design the framework of formal investor relations of listed companies to limit risk, especially through the proper fulfilment of the information requirements (Przewodnik, 2015). Among those requirements there is, among others, drawing up and making public the so-called disclosure documents. Alternative Trading System Regulations (Regulamin, 2015) defines the requirements to be met by disclosure documents. It requires, among others, the section "Risk Factors" to include information on the factors causing risk for the buyer of financial instruments included in the disclosure document, in particular factors related to the economic and financial position of the issuer and its capital group (Regulamin, 2015).

The first and already completed phase of the research showed that the most frequently reported type of risk in the surveyed enterprises was risk related to key persons. This risk is indicated in the disclosure documents of 44 out of 50 service companies listed on NewConnect (Jedynak & Jedynak, 2015). Therefore, the author attempted to conduct in-depth research on the essence, content and consequences of the occurrence of that risk.

The research included in its scope the content of disclosure documents prepared by 44 companies representing the services sector, present on the NewConnect (this is the whole population of companies declaring the existence of risk related to key people in their business). The primary objective of the study was to get to know the perception of the risk associated with key people in the surveyed companies.

This objective is developed in the form of the following specific partial objectives:

- Objective 1. Getting to know the ways of determining the essence of risk associated with key people in the surveyed companies.
- Objective 2. Understanding the consequences of the occurrence of risks associated with those key people, as envisaged in the surveyed companies.
- Objective 3. Understanding the importance of key people for the business of the surveyed companies.

8.3. Empirical research results

Table 8.1 shows how the surveyed companies perceive the risk related to key persons.

Table 8.1 *Perception of the risk related to key persons in the surveyed companies*

Company	Identification of the essence of risk																
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
Agroliga Group					x					x				x		x	
Agtes	x		x		x												
Airmarket	x		x		x							x	x			x	x
Analizy Online	x		x					x					x	x		x	
Aqua	x		x		x												
Artefe	x	x	x									x				x	
Art New Media						x											x
Asm Group					x												
Auto-Spa					x												
Atc-cargo	x	x	x	x	x												
Balticon	x	x	x			x									x		
BBC	x		x			x											
Calesco	x		x					x			x						
Copernicus Securities					x		x										
Elektromont			x		x												
Finhouse							x										
Formula8							x								x		
Forposta					x					x							
HRC Grupa	x		x														
Hollywood					x												
Hurtimex	x		x														
IBC Polska F&P					x												
ICP Group	x		x							x							
IPO Doradztwo Strategiczne	x		x			x											
Investeko	x		x		x							x				x	
Kupiec Transport & Spedition	x		x														
Langloo.com	x		x		x		x			x					x	x	
Lauren Peso Polska		x	x									x				x	
Logzact					x												
Marketeo.com	x		x					x									

MM Conferences						x											
Momo S.A.					x												
Morizon.pl			x								x				x	x	
Nemex			x		x								x				
Notoria Serwis	x		x		x												
Polski Holding Rekrutacyjny					x		x										
Prolog	x		x		x							x					
Seka						x						x					
Sescom					x	x				x	x						
Terra	x		x			x											
Verbum	x				x				x								
Viatron	x		x					x									
Wealth Bay		x		x	x	x	x										
Your Image	x	x	x	x													

Legend:

- 1 – loss of people having expertise (P1)
- 2 – loss of people who have developed relationships in the industry (P2)
- 3 – loss of experienced people (P3)
- 4 – loss of people to whom substantial powers have been delegated (P4)
- 5 – loss of management staff (P5)
- 6 – loss of associates, not employed on contracts of employment (P6)
- 7 – loss of a major originator of projects implemented in the company (P7)
- 8 – loss of people trained to use specialized infrastructure (P8)
- 9 – loss of several key people at the same time (P9)
- 10 – loss of people co-creating the competitiveness of company (P10)
- 11 – loss of persons whose education and experience is unique (low supply of employees in the labour market) (P11)
- 12 – loss of employees for whom there is a high demand in the labour market (P12)
- 13 – loss of employees who are able to meet the requirements of customers (P13)
- 14 – loss of key people with high salary demands (P14)
- 15 – problems with recruitment (P15)
- 16 – loss of employees as a result of increased competition among employers on the labour market (P16)
- 17 – loss of employees due to the lack of possibility of pursuing a career in the company (P17)

The research conducted helped identify 17 definitions of risk associated with key people relating to the surveyed companies. They highlight the complexity of content that is within the scope of this concept. The analysed risk is most often equated with the loss of people with expertise particularly useful for companies, in the form of knowledge and experience (P1 – 23 companies and P3 – 26 companies). The members of the managerial staff (P5 – 23 companies) are relatively often regarded as key persons. It is also worth noting that in the surveyed companies among key people there are also associates who are not employed on a contract of employment (P6 – 9 companies), which is associated with the currently popular use of flexible forms of employment.

A large part of associations (P11 – 2 companies, P12 – 6 companies, P14 – 3 companies P15 – 4 companies P16 – 8 companies and P17 – 2 companies) concerns the risk related to the problems of the occurrence of the surveyed companies on today's labour markets.

On the other hand, Table 8.2 summarizes the potential consequences associated with the occurrence of risk related to key persons, perceived in the surveyed companies.

Table 8.2 *Consequences of the occurrence of risk related to key people predicted in the surveyed companies*

Company	Consequences of risk														
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Agroliga Group	x								x		x				
Agtes											x				
Airmarket														x	
Analizy Online											x				
Aqua							x	x	x						
Artefe											x				
Art New Media									x						
Asm Group			x						x		x				
Auto-Spa	x								x		x				
Atc-cargo											x				
Balticon						x					x				
BBC			x			x			x			x			
Calesco	x													x	
Copernicus Securities	x										x				
Elektromont									x		x				
Finhouse	x														
Formula8							x				x		x		
Forposta									x		x				
HRC Grupa									x						
Hollywood									x		x				
Hurtimex								x			x				
IBC Polska F&P	x								x		x				
ICP Group		x	x						x					x	
IPO Doradztwo Strategiczne									x		x				x
Investeko		x						x	x		x			x	
Kupiec Transport & Spedition		x									x			x	
Langloo.com	x					x						x			

(C3 – 4 companies C4 – 4 companies, C13 – 3 companies and C14 – 8 companies). What was also indicated was the possibility of deterioration in the quality and timeliness of services provided (C7 – 4 companies C8 – 5 companies).

Conclusions

The conducted research on literature and empirical studies allow for formulating the following main conclusions:

- The concept of risk associated with key persons is multi-faceted. This multi-faceted nature manifests itself in the mentioned risk contributing to the creation of the current trends involving the increase of the scale of risk of the business activity conducted as well as potential strategic importance of this risk for the business activity of the organization.
- Risk related to key persons is a very common type of risk among the analyzed service companies. This means that management models of the companies surveyed assume a significant impact of key persons on the course of management processes and delivery of services at all levels of management.
- The essence of risk related to key persons in the analyzed companies is understood very differently. This diversity applies to the terms attributed to employees, allowing them to be considered key. Both executives and specialists are treated as key persons. In the latter case, both a person employed under contracts of employment and those who are employed using flexible forms of employment are indicated.
- The primary source of potential problems with key people is their particularly high level of competence that in the above-average way contribute to the success of the activities of companies and whose loss threatens the possibility of achieving the mentioned success. On the other hand, one can also indicate as a source of problems the current trends prevailing in the labour market that hinder the surveyed companies from retaining key employees.
- The loss of key persons in the surveyed enterprises is accompanied by numerous potentially negative consequences. They concern the problems of a strategic, operational, and personnel nature and those related to results, quality and timeliness of the services provided.

Due to the sampling scheme used, the results of empirical research cannot be the basis for their generalization for the entire population of service companies in Poland. These results, however, present high cognitive, diagnostic and exemplifying qualities. In addition, the research methodology used can provide the basis for its extension and continuation.

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